

**ST 02-29**

**Tax Type: Sales Tax**

**Issue: Reasonable Cause on Application of Penalties**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS**

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**THE DEPARTMENT OF REVENUE  
OF THE STATE OF ILLINOIS**

v.

**COFFEE HOUSE,  
Taxpayer**

No. 01-ST-0000  
IBT# 0000-0000  
Assessment # 00 00000000000000

**Ted Sherrod  
Administrative Law Judge**

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**RECOMMENDATION FOR DISPOSITION**

**Appearances:** Special Assistant Attorney General Marc Muchin on behalf of the Illinois Department of Revenue; John Doe, *pro se* on behalf of Coffee House.

**Synopsis:**

This matter is before this administrative tribunal as the result of a timely protest of an RA-52-05 Notice of Assessment for Form ST-1 issued by the Illinois Department of Revenue (hereinafter referred to as the "Department") on March 27, 2001 assessing a late payment penalty. Coffee House (hereinafter "taxpayer") protested this determination and requested a hearing, which was held on August 30, 2002. Mr. John Doe, the taxpayer's office manager and financial director, appeared and testified at the hearing. Following the submission of all evidence and a review of the record, it is recommended that this

matter be resolved in favor of the Department. In support of this recommendation, I make the following findings of fact and conclusions of law.

**Findings of Fact:**

1. The Department's *prima facie* case against the taxpayer, inclusive of all jurisdictional elements, was established by the admission into evidence of the Department's RA-52-05 Notice of Assessment for Form ST-1 issued March 27, 2001. Dept. Ex. 1.
2. The taxpayer is a corporation engaged in the operation of a restaurant located in Anywhere, Illinois. Dept. Ex. 1.
3. John Doe is the office manager and financial director of the taxpayer. Testimony of John Doe.
4. Jane Doe is a member of the taxpayer's accounting department assigned to assist Mr. Doe with the payment of taxes by electronic funds transfer. Testimony of John Doe.
5. The taxpayer is required to file quarter monthly returns with the Department and to remit taxes by electronic funds transfer. Dept. Ex. 1; Taxpayer's Ex. 1.
6. The taxpayer uses either the Automated Clearing House (ACH) debit or credit method to pay taxes by electronic funds transfer; persons using these methods must initiate electronic funds transfer payments no later than the day before the date on which the payment is to be credited to the taxpayer. Testimony of John Doe; Dept. Ex. 2.
7. The taxpayer was required to deliver taxes due for January, 2001 to the Department on or before February 20, 2001; the taxpayer failed to make this tax payment on or before this due date. Testimony of John Doe; Dept. Ex. 2.

8. The taxpayer attempted to initiate an electronic funds transfer payment on February 19, 2001; it was unable to do so, however, because February 19, 2001 was President's Day, a legal holiday, and the taxpayer's bank was closed. Testimony of John Doe; Dept. Ex. 2.
9. The taxpayer's bank was open February 20, 2001, and the taxpayer initiated its electronic funds transfer payment of its January taxes by ACH debit or credit on this date; this payment was received by the Department and credited to the taxpayer's account on February 21, 2001. Testimony of John Doe; Dept. Ex. 2.
10. On March 27, 2001, the Department issued an RA-52-05 Notice of Assessment for Form ST-1 assessing the taxpayer a late payment penalty and denying the taxpayer a prompt payment discount. Dept. Ex. 1.<sup>1</sup>
11. The taxpayer requested an abatement of the late payment penalty; the Department denied this request "due to poor filing record and no valid excuse." Dept. Ex. 2.

**Conclusions of Law:**

The Department imposed a penalty for late payment of taxes pursuant to section 3-3(b-10) of the Uniform Penalty and Interest Act ("UPIA"), 35 ILCS 735/3-3(b-10) (hereinafter "section 3-3(b-10)"). Section 3-3(b-10) includes the following provision:

This subsection (b-10) is applicable to returns due on and after January 1, 2001. A penalty shall be imposed for failure to pay:

- (1) the tax shown due on a return on or before the due date prescribed for payment of that tax, an amount of underpayment of estimated tax, or an amount that is reported in an amended return other than an amended return timely filed as required by subsection (b) of Section 506 of the Illinois Income Tax Act (penalty for late payment or nonpayment of admitted liability).

35 ILCS 735/3-3(b-10)

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<sup>1</sup> A prompt payment discount is not available on any tax that is paid late. 86 Ill. Admin. Code § 150.905.

The Department's determination is presumed correct. A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826 (1<sup>st</sup> Dist. 1988). Once the presumed correctness of the assessment is established, the burden shifts to the taxpayer to prove that the determination was in error. Copilevitz v. Department of Revenue, 41 Ill. 2<sup>nd</sup> 154 (1968); Central Furniture Mart v. Johnson, 157 Ill. App. 3<sup>rd</sup> 907 (1<sup>st</sup> Dist. 1987); Vitale v. Department of Revenue, 118 Ill. App. 3<sup>rd</sup> 210 (3<sup>rd</sup> Dist. 1983); Masini v. Department of Revenue, 60 Ill. App. 3<sup>rd</sup> 11 (1<sup>st</sup> Dist. 1978); A.R. Barnes & Co., *supra*.

Section 3-8 of the UPIA, 35 ILCS 735/3-8, provides a basis for the abatement of the section 3-3(b-10) penalty, and states as follows:

No penalties if reasonable cause exists. The penalties imposed under the provisions of section 3-3, 3-4, 3-5 and 3-7.5 of this Act shall not apply if the taxpayer shows that his failure to file a return or pay tax at the required time was due to reasonable cause. Reasonable cause shall be determined in each situation in accordance with the rules and regulations promulgated by the Department. A taxpayer may protest the imposition of a penalty under Section 3-3, 3-4, 3-5, or 3-7.5 on the basis of reasonable cause without protesting the underlying tax liability.

35 ILCS 735/3-8

Pursuant to authority granted by the legislature, the Department has promulgated rules interpreting reasonable cause at 86 Ill. Admin. Code, ch. I, § 700.400. These rules provide in part as follows:

e) Examples of Reasonable Cause. The following non-exclusive list of situations will constitute reasonable cause for purposes of the abatement of penalties ...

7) Reasonable cause will exist for purposes of abatement of the penalty if a taxpayer makes an honest mistake, such as inadvertently mailing a Department of Revenue check to a local government, another state's Department of Revenue, or to the Internal Revenue Service.

86 Ill. Admin. Code, ch. I, § 700.400(e)(7)

The taxpayer contends that its late payment in this case was due to an "honest mistake." The taxpayer inadvertently failed to initiate its electronic funds transfer

(“EFT”) on the business day preceding a holiday in accordance with instructions indicated in the Department’s Form EFT-9. Dept. Ex. 2. This error occurred because Jane Doe, a member of the taxpayer’s accounting department responsible for EFT, did not realize that February 19, 2001 was a legal holiday on which the banks would be closed, making the initiation of an electronic funds transfer on that date impossible. Ms. Jane Doe initiated an EFT payment by ACH debit or credit transfer the following business day, February 20, 2001, which resulted in the receipt of funds from the taxpayer’s bank account by the Department on February 21, 2001. February 21, 2001 was one day after the due date for payment of the taxpayer’s tax due for January, 2001. 35 ILCS 120/3. Accordingly, the Department assessed a late payment penalty pursuant to section 3-3(b-10).

The taxpayer sought an abatement of the penalty assessed, which was denied by the Department. Dept. Ex. 2. During the hearing, the Department indicated that it based its denial of the taxpayer’s request for abatement in part upon the taxpayer’s history of poor compliance. In support of this claim, the Department introduced an MEM-45 Reasonable Cause Protest letter from the Department’s Account Management Division dated December 11, 2001 in which the Department mentions the taxpayer’s “poor filing record.” Dept. Ex. 2. However, the Department introduced no evidence of any specific instances in which the taxpayer had been determined to be delinquent. In rebuttal, the taxpayer introduced documentary evidence that the taxpayer had previously been assessed a late payment penalty in 1999. Taxpayer’s Ex. 1. This evidence showed that the Department subsequently determined that the taxpayer had timely complied and was not delinquent. *Id.* Mr. Doe testified that he was responsible for maintaining the

taxpayer's tax records, that he kept all correspondence from the Department, and that the erroneous assessment introduced into the record was the only instance in which the taxpayer had been accused of failing to timely comply.

In this state of the record, with Mr. Doe' testimony not contradicted and corroborated by documentary evidence, the *prima facie* case that the taxpayer had a poor compliance record made by the Department's assessment determination was overcome. Novick v. Department of Revenue, 373 Ill. 342 (1940). The burden thus shifted to the Department to prove this claim by competent evidence. *Id.* The Department has failed to do this. Accordingly, I find that the Department's determination that the taxpayer had a poor filing record was successfully rebutted.

One of the most important factors to be considered in deciding whether to abate a penalty is the extent to which the taxpayer made a good faith effort to comply. 86 Ill. Admin. Code, ch. I, § 700.400(b). A taxpayer will be considered to have made a good faith effort to comply if it exercised ordinary care and prudence in doing so. 86 Ill. Admin. Code, ch. I, § 700.400(c). A taxpayer's filing and payment history is a fact properly taken into account when considering whether a taxpayer has made a good faith effort to file its return in a timely fashion. 86 Ill. Admin. Code, ch. I, § 700.400(d). The taxpayer's prior filing history, therefore, mitigates in favor of the taxpayer. However, while a good compliance record is a factor to be considered, evidence of a good compliance record alone is not sufficient to show reasonable cause if other factors indicate that the taxpayer did not exercise ordinary care and prudence in attempting to comply with Illinois law.

In this case, the record shows that the taxpayer was required to pay taxes by electronic funds transfer.<sup>2</sup> Persons mandated to pay in this manner must register with the Department and complete and execute an EFT-1 Authorization Agreement for Electronic Funds Transfer. 86 Ill. Admin. Code, ch. I, § 760.220. This form would have been forwarded to the taxpayer along with forms and instructions sent to all EFT filers.

While the taxpayer contends that these materials were never received, 86 Ill. Admin. Code, ch. I, § 700.400(f)(5) on “Reasonable Cause” states “(I)n the absence of new or unusual circumstances, most filing and payment requirements are common knowledge or are readily available to most taxpayers.” The taxpayer presented no evidence of unusual circumstances, such as a change of address or other problems with the receipt of mail, that would explain why these instructions would not have been received. Moreover, during the hearing the taxpayer acknowledged that these instructions might have been received by Ms. Jane Doe and misplaced or ignored. Given this evidence, I conclude that the taxpayer received the Department’s forms and instructions, including the Department’s Form EFT-9.

The type of information that is available to a taxpayer is a fact that is relevant to whether it exercised ordinary business care and prudence. See 86 Ill. Admin. Code, ch. I, § 700.400 (b), (c). For the reasons noted above, I find that the taxpayer had access to the Department’s forms and instructions pertaining to electronic filings. One such form is the Department’s Form EFT-9 entitled “Electronic Funds Transfer Observed Holidays.” Dept. Ex. 2. This form states that February 19, 2001 is a legal holiday and outlines in

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<sup>2</sup> Taxpayers who have an annual tax liability of \$200,000 or more must send payment by electronic funds transfer. 35 ILCS 120/3.

detail procedures to be followed when an EFT due date falls on, or the day after a holiday. Specifically, this form states:

If the due date is the **day after** a weekend or Federal Reserve holiday, you must complete your EFT transaction at least one day before the weekend or holiday. If you do not, your payment will not be credited to the state's account on the statutory due date and you may be assessed penalties and interest. For example, if your payment is due on Monday, August 20, 2001, you must complete your transaction on Friday, August 17, 2001.

Department Form EFT-9

Since the taxpayer was placed on notice that February 19, 2001 would be a holiday, and that its EFT transfer would only be timely if initiated on the preceding business day, the taxpayer's mistaken belief to the contrary was unwarranted. Since the taxpayer chose to discard or ignore the Department's clear instructions contained in its form EFT-9, I do not find the taxpayer's failure to comply to be an "honest mistake." To hold otherwise would improperly absolve the taxpayer of responsibility for retaining and following the instructions contained in the Department's forms and manuals, which is the essence of the exercise of ordinary care and prudence in fulfilling compliance obligations.

Even if this tribunal accepted the taxpayer's explanation that the bank was closed on February 19, 2001 as a legitimate excuse for its failure timely pay its tax by February 20, 2001, this only explains why payment could not be timely made using an ACH debit or credit procedure. It does not explain why the taxpayer failed to complete its wire transfer on the due date by making a fedwire transfer that could be initiated and completed on February 20, 2001, when the bank was open. The Department's regulations, which have been in effect since 1993, clearly authorize the use of fedwire procedures when doing so is the only way to avoid a late payment penalty. See 86 Ill. Admin. Code, ch. I, § 750.600. Had the taxpayer called the Department's EFT telephone



number indicated in the Form EFT-1 the taxpayer received, and explained its situation on February 20, 2001, the taxpayer would have been instructed to utilize this procedure to avoid a penalty. *Id.* Since the taxpayer's bank was open on February 20, 2001, the taxpayer's failure to utilize the fedwire transfer procedure to avoid a late payment penalty cannot be excused by the bank's closure on February 19, 2001.

**WHEREFORE,** for the reasons stated above, it is my recommendation that the Department's late payment penalty assessment be upheld and that the RA-52-05 Notice of Assessment for Form ST-1 issued to the taxpayer on March 27, 2001, be finalized as issued.

Date: September 13, 2002

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Ted Sherrod  
Administrative Law Judge